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DEPT FOR AF/E, AF/RSA, AND EB/CBA
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DEPT ALSO PASS TO USTR FOR BILL JACKSON, KARL TSUJI, AND
JEAN KEMP
TREASURY FOR LUKAS KOHLER
DOC/ITA FOR ROBERT TELCHIN AND RASHIDA PETERSEN

SIPDIS

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TAGS: BEXP ETRD EINV EAID ECON KE
SUBJECT: Embassy Urges Ex-Im Support for Locomotive Export
to Magadi Soda in Kenya

REF: Ex-Im Bank Economic Impact Analysis: AP081717XX

(Kenya-Soda Ash)

¶1. Summary: Ex-Im rejection of U.S. producer NREC's application for support for sale of eight locomotives to Kenya's Magadi Soda would contradict U.S. policy to help African countries expand their foreign trade, and produce a terrible optic for the USG. Embassy questions Ex-Im's projection that Magadi Soda's increased exports would reduce potential U.S. soda ash exports by $24.6 million over six years, given the high growth in domestic demand. It is also questionable that U.S. industry would suffer any damage, given rising world prices. Magadi's exports are too small to significantly impact U.S. industry, but boosting them would assist Kenya's efforts to reduce widespread poverty and unemployment. Rejecting the application would also miss an opportunity for NREC to break into a growing market and encourage Magadi and other East African firms to buy European or Chinese railroad equipment instead. End summary.

NREC/Magadi Soda Application

¶2. Ex-Im Bank has received an application to support the $14.4 million export by National Railway Equipment Company (NREC) of Mt. Vernon, IL of eight (8) refurbished locomotives to Magadi Railway, a captive railroad of Magadi Soda Company (MSC), of Kenya. The locomotives are valued at $14.4 million, and Ex-Im Bank estimates that NREC will also sell an additional $1.4 million in spare parts, for total U.S. exports of $15.8 million. The locomotives will be integral to Magadi's 365,000 metric ton/year soda ash expansion project expected to commence in late 2006. Ex-Im's analysis estimates the expansion in Magadi's exports will cause U.S. soda ash producers to lose a projected $24.6 million in exports over six years, making it likely Ex-Im will reject the application.

¶3. U.S. Embassy Nairobi's FCS and the Economic Sections have reviewed Ex-Im's Economic Impact Analysis for Magadi Soda Company's application. It seems much more likely that the positive impact on the U.S. economy as a result of increased locomotive manufacturer's business will equal or exceed any negative impact on U.S. soda ash industry exports. We offer the following observations and comments.

Projected Export Loss Figure Appears Too High

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¶4. It is reasonable to question this "projected export loss" figure. Repair of hurricane damage has caused tight supplies of glass and other construction material. With forecasts for future active hurricane seasons boosting domestic demand, we question the claim that Magadi could displace 48,930 tons of U.S. exports worth $24.6 million, which would represent only 1.06% of U.S. soda ash exports. The report itself indicates that U.S. demand is growing faster than expected. It is possible, if not likely, that Ex-Im's estimate of displaced U.S. soda ash exports is a "worst case" scenario unlikely to be realized.

¶5. Magadi exports 90% of its current production (350,000 tons of soda ash per year), or only 315,000 tons. This is only 0.75% of the 42 million tons of world soda ash production in 2005. When U.S. industry exports 4.6 million tons a year and is by far the world's largest exporter, Ex-Im Bank rejection of something as modest as routine assistance in support of a U.S. manufacturer for locomotives to a relatively tiny (less than 1%) producer in a struggling, developing country such as Kenya would appear to be in direct conflict with the USG goal to help countries like Kenya with economic development.

¶6. If it is true, as the report states, that since 2003 soda ash demand has grown between 3-4% per year and is forecast to continue growing at that rate through 2010 -- and that prices are expected to increase in the 25-30% range -- then "all the boats are rising" and U.S. industry should have nothing to fear from a very modest increase in activity by Magadi. In 2005, the U.S. supplied 26% of the world's soda ash, with 60% of its total production being consumed domestically and 40% (the 4.6 million tons mentioned above) being exported. Magadi's exports are

only 1/15 of U.S. exports. Magadi's exports to Asia, where most growth is expected, are only 1/70th those of U.S. exports.

¶7. Competitive "issues" in the application exist. However, particularly given the huge advantages the U.S. enjoys in terms of scale, quality, productivity, infrastructure, etc., the relative size of those "issues" appears insignificant compared to the certain benefits to U.S. manufacturers, associated service providers (e.g., shipping and insurance), Kenyan economic growth, and an enhanced U.S.-Kenya relationship overall.

¶8. A global commodities boom and 25-30% increase of U.S. soda ash prices in 2004 and 2005 led U.S. producers to re-open closed plants, and since 2003 the U.S. soda ash industry has been running at 100% capacity. Major consumers of soda ash, especially in the U.S., reported sold-out conditions in 2005, causing the U.S. flat glass industry to express concern about the availability of this crucial raw material. In short, the outlook for the U.S. and global soda ash industry has never been more positive. Under these conditions, a refusal to help both U.S. manufacturer (in much more tenuous economic conditions) AND a developing might be tough to defend in the court of global public opinion, and would hurt the U.S. image in East Africa.

Ex-Im Analysis Omits Additional Benefits of Project
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¶9. The analysis appears to overlook the following additional benefits of supporting Magadi's loan application.

¶10. Creation of additional business for NREC and other U.S. locomotive and equipment suppliers over the 6-year repayment period from other markets/industries in Africa -- and thus additional dollars and jobs for the U.S. locomotive industry. Expanded and improved rail service is

potentially a good growth sector in Africa, particularly in freight, when much of the world will likely be experiencing flat growth rates. Mombasa is East Africa's gateway to the world, and the recent concessioning of the Kenya-Uganda railway should restore the dilapidated railroad to play a critical role in relieving freight congestion, cutting transport time/costs, and stimulating economic growth.

¶11. U.S. heavy equipment and vehicle manufacturers are not well represented in Kenya or most of Africa and face very strong competition from traditional European and very aggressive Chinese manufacturers. With improvements planned for the existing Mombasa-Kampala rail line, and serious studies being undertaken on extending rail service to southern Sudan, East Africa is potentially an important market for locomotive and other rail equipment manufacturers. NREC's contract with Magadi would be a strong advertisement and toehold in a new market. U.S. firms should be supported in pursuing opportunities in this region. (USTDA is also studying significant expansions of rail freight in Senegal). If Ex-Im rejects Magadi's application for financing, Magadi may simply buy equipment from Europe, Japan or China, which will deny the U.S. any export benefit, and still leave U.S. soda ash producers facing Magadi.

¶12. We urgently need a U.S. "success story" in Kenya. The Boeing sale was a once-in-twenty years one-off -- and may not create as many jobs in Kenya as the Magadi project.

Rejection of Application Inconsistent with USG Policy Goals

¶13. The U.S. has a stated foreign policy to assist emerging African countries, and their producers, to improve and enhance their foreign trade as the most effective means of attracting investment, creating jobs and fighting poverty. Fully integrating African countries into the benefits of enhanced world trade is a U.S. priority. Currently, the entire continent of Africa accounts for only 2% of global trade. Ex-Im rejection of the application would create a terrible optic that would contradict the stated policy.

¶14. Looking at the bigger picture, the possibility of more failed or failing states in Africa is a real concern. We all know that these environments are the best safe havens for terrorists. Kenya has so far proved itself willing to democratize at a faster pace than most other African countries. It remains a poor country, however, in which 56% of the population lives on a dollar a day or less, and in which unemployment is estimated to be 50%. It should be supported, primarily through any viable trade and investment vehicle available. We have already seen that U.S. support of successful private sector companies leads to innumerable positive spin-off effects, an excellent being, to use the example again, Kenya Airways which is today a truly world class airline in part due to its fleet of 100% Boeing aircraft.

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